



County of Los Angeles CHIEF EXECUTIVE OFFICE

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WILLIAM T FUJIOKA
Chief Executive Officer

February 22, 2011

To: Mayor Michael D. Antonovich
Supervisor Gloria Molina
Supervisor Mark Ridley-Thomas
Supervisor Zev Yaroslavsky
Supervisor Don Knabe

From: William T Fujioka
Chief Executive Officer

A handwritten signature in black ink, appearing to read "W. T. Fujioka", is written over the printed name and title.

Board of Supervisors
GLORIA MOLINA
First District

MARK RIDLEY-THOMAS
Second District

ZEV YAROSLAVSKY
Third District

DON KNABE
Fourth District

MICHAEL D. ANTONOVICH
Fifth District

RESPONSE TO BOARD ORDER OF JANUARY 18, 2011 TO MONITOR MUNICIPAL BANKRUPTCIES IN THE UNITED STATES THAT WOULD HAVE A DIRECT IMPACT ON OUR MUNICIPALITIES AND REPORT BACK ON THE COURT DECISION ON THE CITY OF VALLEJO BANKRUPTCY PLAN

On January 18, 2011, Mayor Antonovich requested the Chief Executive Office to monitor municipal bankruptcies in the United States that would have a direct impact on our municipalities and report back on the court decision on the City of Vallejo bankruptcy plan.

Overview

California Law

Existing law grants local public agencies in California broad access to Federal bankruptcy. The State statutes addressing municipal bankruptcy in California were first enacted under SB 338 of 1939. SB 768 of 1949 codified the State statutes which authorize bankruptcy filings by local governments.

In 2001, after studying existing statutes authorizing bankruptcy filings by local public entities, the California Law Revision Commission recommended revisions to conform the statutes to Federal bankruptcy laws and to reaffirm the intent of the statute to provide the broadest possible access to municipal debt relief under Federal law. Legislators approved the Commission's recommendations the following year (SB 1323, Chapter 94, Statutes of 2002).

"To Enrich Lives Through Effective And Caring Service"

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Federal Law

Under existing Federal law, states do not have the right to file for bankruptcy and there are no bills currently being considered by Congress to amend the United States Bankruptcy Code to allow states the ability to file for bankruptcy.

According to the Federal Bankruptcy Court, in more than 60 years since the Congress established a Federal mechanism for the resolution of municipal debts, there have been fewer than 500 municipal bankruptcy petitions filed. Although similar to other bankruptcy provisions, Chapter 9 of the United States Bankruptcy Code is significantly different, in that, there is no provision in the law for liquidation of the assets of the municipality and distribution of the proceeds to creditors. Chapter 9 establishes several conditions before a municipality may file for bankruptcy. The municipality: 1) must be insolvent; 2) must have trouble securing agreements from creditors; and 3) must be specifically authorized by the state to file for bankruptcy.

Recent Developments

House Oversight Committee Examines State and Municipal Debt Situation

On February 9, 2011, the Subcommittee on Financial Services and Bailouts of the House Oversight and Government Reform Committee held an informational hearing titled, "State and Municipal Debt: The Coming Crisis?" The purpose of the hearing was to understand the municipal debt crisis facing state and local governments, to assess its causes, and to consider available solutions. Committee members discussed possible scenarios if a state simply defaulted on some or all of its obligations, declaring itself unable to pay. However, no conclusion was reached as to recommendations for introducing a Federal bankruptcy bill.

Other Recent Developments

- The Center on Budget and Policy Priorities recently reported that 44 states and the District of Columbia are projecting budget shortfalls totaling \$125.0 billion for the upcoming fiscal year, which in most states begins in July, 2011.
- On January 24, 2011, U.S. House Majority Leader Eric Cantor (R-Va) stated that he opposes changing the Federal bankruptcy law that would allow fiscally pressed states to seek bankruptcy protection. Mr. Cantor also stated that there will not be a Federal bailout of states and state governments should not expect Washington to solve their fiscal problems. Additionally, Senate Minority Leader Mitch McConnell (R-Ky) indicated that he opposes state bailouts.

- In response to the possible introduction of Federal legislation by the Congress to allow states to file for bankruptcy, California Treasurer Bill Lockyer responded that states did not ask for such law, do not want it and do not need it. Mr. Lockyer added that bankruptcy would devastate states' ability to recover from the recession and it would inflict severe injury on taxpayers. Further, he added that advocates of this idea confuse states' near-term budget deficits with long-term funding obligations. The latter, including pension obligations, are serious problems, but states are dealing with them by reducing benefits and increasing employees' contributions. With respect to budget shortfalls, states have the tools to fix them without declaring bankruptcy.

City of Vallejo

The City of Vallejo filed for bankruptcy in 2008. On January 18, 2011, the City filed a Plan For the Adjustment of Debts with the United States Bankruptcy Court. Submission of the plan is one of the final steps before the City can emerge from bankruptcy. The City's plan proposes to renegotiate labor contracts with its employee groups; develop a new employee benefits structure; reduce pension, retirement, health, and other benefits; and restructure capital and infrastructure projects.

According to documents submitted to the United States Bankruptcy Court, after several years of struggling to balance inadequate revenues with increasing expenditures, the City of Vallejo confronted the reality that it would be unable to pay its bills in early 2008. The City was driven to bankruptcy by a combination of declining tax revenues, as a result of the economic and housing market decline, and the rising cost of contracts with employee unions.

The United States Bankruptcy Court has calendared a hearing for March 7, 2011 in which the Court will review the City of Vallejos' bankruptcy plan.

We will continue to monitor municipal bankruptcy developments and will provide you with updated information regarding the Federal courts' decisions regarding the City of Vallejo.

WTF:RA
MR:RM:er

c: Executive Office, Board of Supervisors
County Counsel